No. 87-562

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

SECURITIES INDUSTRY ASSOCIATION,

Petitioner,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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Respondents argue that *certiorari* is not warranted because (a) the opinion below did not restrict the reach of the Glass-Steagall Act only to securities transactions in the primary (new issue) market and (b) the type of securities activities sanctioned here, like those approved in *Schwab*, do not involve the type of promotional conflicts the Court has held the Act to prohibit. But respondents avoid the fundamental basis of the opinion below and elide the most relevant aspect of the activities involved.

1. The court below *did* construe the Act as reaching only activities in the primary market, contrary to the prior decisions of the Court and the Board. The premise of the lower court's entire statutory analysis was that the Act encompasses only entities that "either purchase securities from the issuer or act as the agent of the issuer" (Pet. App. 9a)—primary market

activities.[1] The court's only passing reference to what could be construed as secondary market activities (14a) was in the context of its hazards discussion, not its analysis of the Act's terms, and even then the reference was simply to what *this* Court had said. The Court as well as the Board have made clear the Act does apply to securities "dealing" in the secondary (trading) market and not simply to new issue activities in the primary market. *See* SIA Pet. 10.

2. The activities sanctioned below *do* give rise to just the sort of promotional conflicts the Act sought to prohibit. These activities plainly are not the same as those approved in *Schwab*. There, the broker engaged only in the execution of securities trades upon the "*unsolicited*" order of customers and "*without* provision of investment advice," which activities the Court found to be within the Board's long-standing interpretation excluding from the Act's coverage brokers "engaged *solely* in executing orders." *See* SIA Pet. 7, 11 n.15. Here, in dispositive contrast, the broker engages in much more than executing unsolicited orders on behalf of others. Not only does it solicit trades in particular securities but in significant part its business also comprises nothing less than *dealing* in securities.

Respondents concede, as they must, the bank affiliate here will promote in this country securities underwritten and/or held by its large overseas merchant banking affiliate. *See* Fed. Mem. 7 n.3; Bk. Mem. 15. When the affiliate acts as the local sales outlet for such securities, it unquestionably has a promotional interest in them extending beyond the prospect of brokerage commissions. As an integrated entity, NatWest stands either to make a mark-up or to avoid a loss on the securities sold. It is therefore not "a matter of indifference" (*ICI*, 401 U.S. at 636) which securities are traded through the

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1 The government's opposition acknowledges this by arguing that the opinion below was correct because the entity here "will not engage in underwriting activities" (Fed. Mem. 5). Yet, incongruously, the government contends that the lower court did not restrict the statute solely to primary market activities. *Id.* n.2.

affiliate. Nor, contrary to respondents, will the revenue yielded to NatWest depend solely on the volume of the shares purchased through CSC, rather than the identity of the shares so purchased. True, CSC may *also* make commissions on unsolicited trades, but to focus exclusively on those commissions, as do respondents, is to overlook the whole point of this case. The issue in this litigation arises from trades that *are* solicited rather than from those that are not.

That the activities here may involve promotion of securities of foreign issuers has particular Glass-Steagall significance, in that one area of specific concern to the Glass-Steagall Congress was bank abuses in the sale of securities of foreign issuers. *See, e.g.*, W. Peach, *The Security Affiliates of National Banks* 115-16 (1941). Further, regardless of the origin of the securities promoted, Congress found "the role of a bank as a promoter of securities" to be "fundamentally incompatible" with its banking obligations. *Bankers Trust*, 468 U.S. at 154. A banking entity, as here, with "a pecuniary incentive in the marketing of a particular security" has "precisely the conflict of interest" Congress meant to eliminate. *Id.* at 156.[2]

In sum, the opinion below contravenes the Court's prior Glass-Steagall admonitions by constricting the scope of the Act only to primary market activities and permitting the Board to sanction through regulation securities activities Congress prohibited by statute.

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2 Respondents' reliance upon *ICI* II to argue the contrary (*e.g.*, Fed. Mem. 6 n.3) is misplaced. There, the Court upheld a bank affiliate's offering investment advice to a closed-end fund precisely because the affiliate did *not* "participate in the sale or distribution of the investment company's securities." 450 U.S. at 52. Here, the sale of securities held by the merchant bank affiliate will be an integral part of CSC's business.

CONCLUSION

For the reasons set forth above and in the Petition for Certiorari, a Writ of Certiorari should issue to review the judgment and opinion of the court below.

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Respectfully submitted,

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